

A fraternal beneficiary society operating under the 'lodge system' has two classes of members, beneficial and social. Beneficial memberships are only available to persons joining prior to their fiftieth birthday, and entitle such members to receive sick, accident and death benefits. Persons joining at age 50 or over are accepted only as social members and are not eligible for benefits. The benefits fund from which payments are made is maintained solely by contributions and dues paid by beneficial members and is segregated from the organization's general funds. Most of the organization's members are beneficial members. Held, the organization is entitled to exemption from Federal income tax as an organization described in section 501(c)(8) of the Internal Revenue Code of 1954.

Advice has been requested as to whether an organization which provides benefits of the type described in section 501(c)(8)(B) of the Internal Revenue Code of 1954, for most but not all of its members, is entitled to exemption from Federal income tax as a fraternal beneficiary society described in section 501(c)(8) of the Code.

Section 501(c)(8) of the Code describes an exempt fraternal beneficiary society as one which: (A) operates under the lodge system or for the exclusive benefit of the members of a fraternity itself operating under the lodge system, and (B) provides for the payment of life, sick, accident, or other benefits to the members of the society or their dependents.

Section 1.501(c)(8)-1 of the Income Tax Regulations provides as follows:

(a) A fraternal beneficiary society is exempt from tax only if operated under the 'lodge system' or for the exclusive benefit of the members so operating. 'Operating under the lodge system' means carrying on its activities under a form of organization that comprises local branches, chartered by a parent organization and largely self-governing, called lodges, chapters, or the like. In order to be exempt it is also necessary that the society have an established system for the payment to its members or their dependents of life, sick, accident, or other benefits.

(b) To be exempt a fraternal beneficiary society must be operated in furtherance of its fraternal purposes and may not engage in business activities of a kind carried on for profit, except that the carrying on of activities which raise revenues from members and their guests will not deprive the society of its exemption.

The organization meets all the requirements of a fraternal beneficiary society described above, except for the question concerning limitations on the rights to beneficial membership.

Specifically, the general laws of the organization provide for two classes of membership, beneficial and social. Beneficial membership is available only to a member who joins the organization prior to his fiftieth birthday, and entitles the member to sick, accident and death benefits, in addition to normal club privileges. Social membership is available to any member who wishes it, but is the only class of membership available to a member who joins the organization on or after his fiftieth birthday. Social membership carries all club privileges but does not confer any sick, accident or death benefits.

The fund from which benefits are paid to beneficial members is contributed to solely by those members and is kept separate and apart from the general funds of the organization. Contributions to the fund by beneficial members are in the form of increased dues which are in addition to other dues and assessments paid by all classes of members. Substantially all of the organization's members are beneficial members.

In view of the above-quoted provisions of the Code and regulations, the question arises whether a provision in an organization's bylaws, etc., to restrict benefit payments to a certain membership class is in conflict with the requirements for exemption under section 501(c)(8) of the Code.

In the case of Polish Army Veterans Post 147 v. Commissioner, 24 T.C. 891 (1955), affirmed 236 F. (2d) 509 (3rd Cir. 1956), approximately 90 percent of the members were not entitled to receive benefits provided by the organization. In support of its conclusion that the organization was not entitled to exemption under section 101(3) of the Internal Revenue Code of 1939, which corresponds to section 501(c)(8) of the Internal Revenue Code of 1954, the Tax Court of the United States stated that-

\* \* \* an organization does not qualify as a 'beneficiary' society where most of its members are not entitled to receive any benefits. (*Italic supplied.*)

The court in that case also found that funds for payment of benefits to beneficial members were derived in part from dues and income received from members who were not entitled to receive any of the benefits provided by the organization.

In view of the Tax Court's interpretation of the requirements of section 501(c)(8) of the Code, it seems reasonable to assume that exemption is not precluded where most of the members of an organization are eligible to receive the benefits provided by the organization, and the benefits are paid from a separate fund maintained solely by contributions or dues paid by the beneficial members for that purpose. Furthermore, in the cited case, no reason was given in explanation of the creation of a nonbeneficial class of membership, while in the instant case the age restriction on beneficial membership appears

to have been included in the general laws of the organization to discourage membership by persons desirous of joining after age 50 who are principally interested in obtaining these benefits rather than in furthering the fraternal purposes of the organization. Under these circumstances, all members are considered to be participating in the fraternal aspects of the organization.

In view of the foregoing, it is held that the organization is entitled to exemption from Federal income tax as an organization described in section 501(c)(8) of the Code.

However, an organization which does not meet all other requirements for exemption under section 501(c)(8) of the Code will not qualify for exemption under that section even if substantially all of the members are entitled to receive benefits of the type described in section 501(c)(8)(B) of the Code. Fraternal Order of Civitans of America, 19 T.C. 240 (1952).

An organization which considers itself within the scope of this Revenue Ruling must, in order to establish exemption under section 501(c)(8) of the Code, file an application on Form 1024, Exemption Application, with the District Director of Internal Revenue for the internal revenue district in which is located the principal place of business or principal office of the organization, unless it is included in a group ruling issued to a parent organization of which it is a subordinate unit. See section 1.501(a)-1 of the regulations.